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Another Failed Defense of the Jones Act

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As the Cato Institute continues to press the case for Jones Act reform, defenders of this flawed and failed law have repeatedly made clear that they've taken notice. Fresh evidence of this was seen earlier this month with the publication of an op-ed on the leading maritime website gCaptain.com. Entitled "CATO's Continued Attempt to Skin the Jones Act," the piece was an obvious preemptive salvo launched a day prior to Cato's recent conference on the law's shortcomings. A close reading, however, reveals it to be another instance of Jones Act defenders missing the mark.

Examining the law's history, author Sal Mercogliano—a professor at Campbell University—claims that prior to the outbreak of World War II that "the Jones Act, reinforced by the Merchant Marine Act of 1936 ensured that not only was there a domestic shipbuilding industry, but it could be ramped up to support the building of over 5,000 merchant ships…" This is, at best, incomplete. As the book Global Reach points out, during this time U.S. merchant shipbuilding was almost non-existent and the fleet itself in obvious decline:

By the mid-1930s American merchant shipbuilding had come to almost a complete halt. In the nearly twenty years following the end of World War I, America's merchant fleet, including its cargo and passenger ships, was becoming obsolete and declining in numbers; nearly 90 percent of the merchant fleet was more than twenty years old, and few ships could do more than ten or eleven knots. Although the Maritime Commission established by the Merchant Marine Act of 1936 had planned to build 50 ships a year under its CDS provisions, by 1939 the United States had only about 1,340 cargo ships and tankers, fewer than the total built by U.S. shipyards in 1914-17, even accounting for wartime losses. In no respect was the U.S. commercial industry capable of meeting the demand for sealift posed by the looming conflicts in Europe and the Pacific.

It's also worth pondering why, if the Jones Act should be regarded as a success, the Merchant Marine Act of 1936 was even needed.

Dr. Mercogliano's explanation of stupefying U.S. shipbuilding costs—commonly estimated to be three to five times greater than those of Asian shipyards—similarly leaves much to be desired:

CATO contends that the Jones Act is a burden that American can no longer bear. Specifically, they cite the higher cost to build ships in America as opposed to overseas. The largest builders of commercial ships in the world today are the Republic of Korea, the People's Republic of China, and Japan; nine out of every ten ships afloat are built in East Asia. The question that needs to be raised is why? It is the exact reason that the CATO Institute rails about with the United States – government subsidies. The South Korean government announced the injection of over $700

million dollars into Hyundai Merchant Marine to stabilize the largest Korean shipping line. It was announced that the South Korean government would be infusing over $1 trillion into shipbuilding, in violation of the World Trade Organization.

While it is true that Asian shipbuilders receive government largesse, both the amount and its alleged explanatory power are vastly overstated. The $1 trillion figure cited—a stunning two-thirds of South Korea's GDP—has no basis in reality. In fact, a recent WTO case brought by Japan against South Korea over its shipbuilding subsidies uses the figure of $11 billion in financial assistance.

The main reason why U.S. shipyards are so wildly expensive is not subsidies but scale. Asian shipyards have it, while U.S. shipyards—where annual output of tankers and cargo ships is typically in the single digits—do not. As this 2015 National Defense University (NDU) report on the U.S. shipbuilding sector explains:

Many of the successful foreign shipbuilders enjoy significant economies of scale from commercial market share dominance. The Jones Act does not deliver the market share necessary for the United States to achieve competitive economies of scale and, therefore, the United States will likely never be competitive in the global commercial market.

A 2009 NDU report similarly held the Jones Act at least partly responsible for U.S. shipyards' lack of competitiveness:

Regarding the international market for commercial ships, U.S. shipbuilders face steep competition from shipbuilders in Asia who offer lower prices, are more efficient, and have higher industry best practice ratings. This is particularly true for the construction of vessels over 1,000 tons. This can be partially attributed to protectionist policies, such as the Jones Act, that have shielded domestic shipbuilders from the pressures of global competition. Thus while U.S. shipbuilders have remained competitive within the U.S. market, they were less so compared to foreign shipyards. None of the shipyards that the Industry Study Team visited expressed confidence that U.S. shipyards, as they are currently configured, could compete effectively in the global shipbuilding market.

Furthermore, the United States is hardly innocent in this regard. As yet another NDU report points out, the Philly Shipyard alone has received "approximately $500 million in direct subsidies and leases its facility from the city for only $1 per year" while the Austal shipyard in Alabama and VT Halter shipyard in Mississippi have received millions more.

There's also the small matter that the Jones Act itself, which mandates the purchase of U.S.-built ships, functions as a massive de facto subsidy scheme.

And for all of the finger pointing at foreign subsidies, it's instructive that when the Clinton administration reached an international deal for an end to shipbuilding subsidies—one that included Japan and South Korea—U.S. shipbuilders performed an about face and turned it down. One would expect a rather different response if subsidies were indeed the decisive factor preventing these shipbuilders from competing with their foreign counterparts.

Mercogliano later goes on to discuss the Jones Act's national security justification and the heavy U.S. reliance on foreign-flagged shipping during Operations Desert Shield and Desert Storm. While conceding that, despite having the Jones Act in place, the conflict "highlighted a shortfall

in American sealift capacity," Mercogliano seems to argue that this had largely been remedied by the time of the 2003 Iraq War with "all the cargo shipped to that conflict [going] on ships crewed by American merchant mariners."

Other sources, however, paint a rather different picture. According to a 2009 Naval War College paper the shipping situation was in fact arguably even more dire than during Desert Shield/Storm:

With 77.6 percent of cargo being moved by United States government owned vessels, TRANSCOM still had to turn to the United States and foreign flagged merchant fleets during the deployment of OIF. In fact, since the United States flagged merchant fleet continued to decline between Desert Shield/Desert Storm and OIF, United States flagged merchant vessels delivered only 1.3 million square feet or a mere 6.3 percent of OIF deployment cargo. Therefore, even with TRANSCOM's high priority of funding after Desert Shield/Desert Storm they were still required to use foreign flagged merchant vessels to move 3.3 million square feet or 16.0 percent of OIF deployment cargo.

While this looks like an 11 percent improvement from Desert Shield/Desert Storm, OIF required 12.1 million square feet less of cargo. Therefore, if the required cargo to be moved was equal to that of Desert Shield/Desert Storm then foreign flag vessels would certainly have been used to carry the majority of the additional cargo. In fact, using a conservative estimate of foreign flag vessels picking up 50 percent of the difference in cargo between the two conflicts would have brought the percentage of cargo carried by foreign flag vessels to 28.6 percent, one percent higher then (sic) during Desert Shield/Desert Storm.

Since this time the Jones Act fleet has only further deteriorated. When Operation Iraqi Freedom began in 2003 the number of Jones Act ships stood at 151. Today it is a mere 98.

None of this is to suggest that the piece is entirely devoid of useful facts or information. Mercogliano, for example, notes that the Jones Act's namesake, Sen. Wesley Jones of Washington state, was "particularly interested in the cabotage provision between his home state and the Alaska territory." This does not surprise, with the Jones Act resulting in two Canadian shipping companies that served Southeast Alaska driven from that market—a development that almost surely benefited competitors in Jones's home state.

Refreshingly, Mercogliano also acknowledges that, should the Jones Act be repealed, "Americans could see a reduction in their freight rates and the opening of new water routes between American ports."

Perhaps most importantly, while he uses his conclusion to oppose repeal of the Jones Act, Mercogliano concedes that reform is needed stating, "Does the Jones Act need reform? Yes, what 98-year-old law does not need updating." We may differ on the exact reforms required, but acknowledging that not all is well with the Jones Act is an important first step.